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SUPREME COURT OF THE UNITED STATES

**OCTOBER TERM, 1943**

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# No. 960

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STANDARD KNITTING MILLS, INC.,
*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE.

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**PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT.**

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The petitioner, Standard Knitting Mills, Inc., prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Sixth Circuit, entered in the above-entitled cause on February 8, 1944, affirming the decision of The Tax Court of the United States, formerly the United States Board of Tax Appeals.

## Opinions Below.

The opinion of The Tax Court of the United States is reported at 47 B. T. A. 295 (R. 47). The opinion of the Court below is not yet reported (R. 142).

## Jurisdiction.

The judgment of the Court below was entered February 8, 1944 (R. 142). The jurisdiction of this Court is invoked

under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925.

**Statutes Involved.**

These are set forth in the Appendix, p. 9.

**Statement of the Case.**

This case involves unjust enrichment taxes under Title III of the Revenue Act of 1936 (c. 690, 49 Stat. 1734, 26 U. S. C. A. — I. R. C. § 700).

The petitioner is a Tennessee corporation, organized in 1900 with its principal place of business in Knoxville, Tennessee. It is engaged in the business of spinning cotton into yarn and knitting underwear and other garments. It was subject to the provisions of the Agricultural Adjustment Act which imposed a processing tax of 4.2 cents per pound on the processing of lint cotton (R. 48).

Because of the tax imposed but not paid for the year 1935, the petitioner filed unjust enrichment tax returns. The first, a tentative return, showed an estimated tax of $5000. The second, a completed return filed February 13, 1937, showed an unjust enrichment tax liability of $38,538.69 (R. 49). The respondent determined that the tax should be $60,200.70, and issued a notice of deficiency showing a deficiency of $21,662.01 (R. 17), from which the petitioner appealed to the Board of Tax Appeals (now The Tax Court) December 13, 1939 (R. 6).

The Board found that a comparison of statutory margins per pound under Section 501(c) of the 1936 Act showed the following (R. 56):

| | |
|---|---|
| Margin in taxable year 1935 | $ .325653141 |
| Average margin 1927-1932 | .270777453 |
| Excess margin | $ .054875688 |

The Board also found that the excess costs of production during the tax period over the base period were $.028528261 per pound (R. 75). To determine the actual extent to which the statutory presumption was rebutted under Section 501(i)(1), the normal and natural procedure would be to subtract the increased costs of production of $.028528261 per lb. from the excess margin of $.054875688 per lb. and arrive at the result $.026347427 per lb. as being the actual extent to which the tax was passed on to others.[1] Instead, however, the Board applied a mathematical formula[2]; and arrived at $.032678799 (R. 75). In the instant case the difference in unjust enrichment tax liability between making the simple subtraction (as was done in the *Regensburg* case with the approval of the Second Circuit), and using the formula (as approved by the Sixth Circuit in the instant case), is approximately $9100.[3]

The Board also made the following findings of fact, but failed to implement such findings by treating them as factors in rebuttal of the statutory presumption under Section 501(i)(1) and, consequently, made no finding as to the actual extent to which such factors established that petitioner has borne the burden of the tax:

1. "During the years 1927 to 1932, inclusive, hereinafter referred to as the base period, petitioner's cotton mill, with

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[1] This is precisely what was done in *E. Regensburg & Sons* v. *Commissioner* (C. C. A. 2, 130 F. (2d) 507); also in *Commissioner* v. *E. Regensburg & Sons* (C. C. A. 2, 139 F. (2d) 883).

[2] The principal point on appeal in *Commissioner* v. *Regensburg, supra*, was the failure to use such a formula. In the Government's brief in that case (p. 24) it is urged:

"The Board of Tax Appeals (now The Tax Court of the United States) has also approved this principle of apportionment in unjust enrichment tax cases arising under Section 501 of the Revenue Act of 1936. See *Stockton* v. *Commissioner*, 44 B. T. A. 514; *Standard Knitting Mills, Inc.* v. *Commissioner*, 47 B. T. A. 295 (on appeal) (C. C. A. 6th)."

[3] In the *Regensburg* case, according to the Government's brief (pp. 22, 25) the difference was $24,560.52 ($36,579.42 minus $12,018.90).

the exception of a portion of 1932, produced coarse carded yarn exclusively, which yarn it knitted into fabric for heavy winter weight garments. It had been making this type of garment for many years *and had practically exhausted means of reducing costs of manufacture by more efficient production methods.* No new style elements could be introduced to increase the demand for the garments. About 1929 the consuming public commenced to demand lightweight underwear and petitioner was required to meet the demand or run the risk of being required to discontinue business. From 1932 to 1935 there was a gradual trend towards slightly lighter weight fabric for underwear. In 1927 about 99 per cent of the petitioner's production consisted of heavyweight garments which were sold on the basis of weight for warmth. The amount decreased to about 40 per cent in 1932 and to about 27 per cent in 1935. *Competition in the heavyweight underwear market increased each year during this period and rendered the business less profitable to petitioner* (R. 50). (Emphasis supplied)

2. "Heavyweight union suits and drawers were the only types of garments manufactured by petitioner during both the base period and in 1935, i.e., common to both periods. *Petitioner did not manufacture any athletic shirts in 1927 and 1928. It produced an experimental quantity in 1929 and attained full commercial production of the garment in 1931. In 1935 about 60 per cent of the garments produced by petitioner were athletic shirts.* Petitioner did not manufacture polo shirts during the base period. It produced 9,352 dozens of that garment in 1935 (R. 50-51). (Emphasis supplied)

3. "Petitioner's employees had to be trained to produce athletic shirts and it was required to develop other means of producing the garments efficiently. Petitioner had devised means of reducing the pounds of material required per

dozen of lightweight garments and the development of high speed sewing machines decreased finishing costs. *These and other savings enabled petitioner to increase its profits per dozen notwithstanding decreased selling prices for the garments* (R. 51). (Emphasis supplied)

4. "The labor costs of the petitioner in 1935 were greater than during the base period on account of provisions of the National Recovery Act enacted in 1933 (R. 51).

5. "The processing taxes imposed upon the petitioner in 1933 were shifted to its customers by adding the taxes as a separate item on invoices. Price lists of petitioner for the fall season of 1934 contained a statement that the price named therein included the processing tax. The desire and intention of the petitioner at that time was to pass the tax on to its customers. Early in 1935 there were pending in various Federal courts suits contesting the validity of the Agricultural Adjustment Act *and by that time customers of petitioner were not disposed to pay processing taxes imposed by the act.* The price list of petitioner for the fall season in 1935 contained nothing about processing taxes (R. 51). (Emphasis supplied)

6. "Petitioner's prices for articles prevail for the entire season unless some important element requires them to be changed. Reductions in selling price generally result in refunds on prior sales during the season. Advances in prices are not retroactive. *More efficient operating methods enabled petitioner to decrease its cost of making lightweight underwear in 1935* (R. 51)."[4] (Emphasis supplied)

The Court below affirmed the decision of The Tax Court and, in doing so, pointedly omitted any discussion of pe-

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[4] Failure and refusal to give effect to similar rebutting factors was the occasion for the reversal and remanding of the case in *E. Regensburg & Sons* v. *Commissioner*, 130 F. (2d) 507. In that case, as in the case at bar, the Trial Court had adopted the view that the *only* rebutting factor that could be given effect was that of increased costs of production.

titioner's Points 3 and 4 (R. 86) under which the petitioner urged it to follow the Second Circuit decision in the *Regensburg* case.[5] The reason now becomes apparent.[6]

Other points urged below (Points 1, 2, 5, R. 86-87) are not pressed here.

**Questions Presented.**

1. Where The Tax Court found that under Section 501(e)(2) there was an excess margin during the tax period of $.054875688 per lb. (indicating that the tax of $.042 per lb. had presumptively been shifted to others), but further found that the increased costs of production during the tax period (over the base period) represented $.028528261 per lb., how are the rebuttal provisions of Section 501(i)(1) to be applied?

2. Where The Tax Court found a marked change in character of the predominant garment manufactured between the base period and the tax period and where it found further (1) that petitioner had devised means of reducing the pounds of material required per dozen garments, (2) that through development of high speed sewing machines it had decreased its finishing costs, and (3) that these and other savings enabled petitioner to increase its profits per dozen notwithstanding decreased selling prices, —are these factors to be considered under Section 501(i)(1) in rebuttal of the statutory presumption?

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[5] 130 F. (2d) 507.

[6] As shedding light on the reason why the Sixth Circuit, in this case, refused to follow the Second Circuit in the *Regensburg* case, the recent decision of the Sixth Circuit in *Cornett-Lewis Coal Co.* v. *Com'r.*, — F. (2d) — (decided April 12, 1944, 44 C. C. H. P. 9281) is illuminating. There, after stating a contention urged as to the meaning of "presumed" in the statute, citing *E. Regensburg & Sons* v. *Helvering*, 130 F. (2d) 507 (C. C. A. 2), the opinion makes the blunt statement, "*We think this view is erroneous.*" (Emphasis supplied)

**Specification of Errors to be Urged.**

The Court below erred:

1. In affirming The Tax Court's holding that Section 501(i)(1) requires the use of a complicated mathematical formula to determine the extent to which the increased costs of production during the tax period rebutted the statutory presumption under Section 501(e) of the 1936 Act.

2. In affirming The Tax Court's failure to give effect, as rebuttal evidence under Section 501(i)(1), to the factors which The Tax Court found as to (1) change in character of the garments, (2) reduction in costs through savings in material, (3) reduction in costs through development of high speed sewing machines and (4) the resulting increase in profits notwithstanding decreased selling prices of garments.

3. In affirming The Tax Court's decision that the petitioner shifted to others the burden of the processing tax to the extent of $70,702.12, and that there was a resulting deficiency in unjust enrichment tax for the year 1935 of $8,301.47.

**Reasons for Granting the Writ.**

The decision below is directly opposed to the construction of identical provisions of the law by the Second Circuit in *E. Regensburg & Sons* v. *Commissioner,* 130 F. (2d) 507, and *Commissioner* v. *E. Regensburg & Sons,* 139 F. (2d) 883. The Court below, in fact, in referring to the first *Regensburg* decision[7] in another case,[8] stated, "*We think this view is erroneous.*" The Second Circuit rule fully supports the petitioner as to each specification of error,

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[7] 130 F. (2d) 507.

[8] *Cornett-Lewis Coal Co.* v. *Commissioner,* — F. (2d) —, decided April 12, 1944.

*supra*. Such a conflict between circuits warrants the exercise by this Court of its power of review under its rules (Rule 38, par. 5(b)).

The decision below ignores the admonitions of this Court, with respect to the consideration and effect which should be given to evidence in rebuttal of the statutory presumption, as stated in *Anniston Mfg. Co.* v. *Davis,* 301 U. S. 337, 351, 355-356. The narrow and stilted construction of Section 501(i)(1) of the 1936 Act by the Court below results in penalizing the taxpayer for its efficiency and in denying due process.

**Conclusion.**

It is respectfully submitted that this petition for a writ of certiorari should be granted.

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April, 1944.